No. 14,953

United States Court of Appeals
For the Ninth Circuit

JOHN O. ENGLAND, Trustee of the Estate of Daniel E. Sanderson, Bankrupt,
Appellant,

vs.

DANIEL E. SANDERSON, Bankrupt,
Appellee.

BRIEF FOR APPELLEE.

JEFFERSON E. PEYSER,
1616 Mills Tower, San Francisco 4, California,
Attorney for Appellee.

LEONARD S. LURIE,
1051 Mills Tower, San Francisco 4, California,
Of Counsel.

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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JURISDICTIONAL STATEMENT.

Appellee accepts the jurisdictional statement of appellant. (Brief, pp. 1-2.)

RESTATEMENT OF QUESTION PRESENTED.

Appellee prefers to restate the question involved before this court as follows: Was the District Court below correct in affirming the order of the Bankruptcy Referee in setting aside to the bankrupt a homestead as exempt "not to exceed $12,500.00 in cash value" (T.R. 18) where at the time of filing of petition in bankruptcy the law of California allowed

a homestead exemption in such sum, or was this error because the bankrupt had one creditor existing at the time of the filing of his petition in bankruptcy who had become such at the time that the homestead exemption was fixed in the sum of $7500.00, all other creditors having become such after the date of the amendment which increased the exemption to $12,-500.00?

STATEMENT OF FACTS.

The facts as stated in appellant's statement of facts are essentially correct and we will accept them as stated rather than to unnecessarily prolong this brief. (Brief, pp. 2-3.)

ARGUMENT.

I. THE COURT BELOW DID NOT ERR IN AFFIRMING THE REFEREE'S ORDER SETTING APART THE HOMESTEAD EXEMPTION IN A SUM NOT EXCEEDING $12,500.00.

The pertinent provisions of the Bankruptcy Act which apply to our problem are the following:

Section 2. (11 U.S.C.A. 11a(11).) This section recites that the courts of bankruptcy are invested with jurisdiction to

> "(11) Determine all claims of bankrupts to their exemptions;"

Section 6. (11 U.S.C.A. 24.)

> "6. This Act shall not affect the allowance to bankrupts of the exemptions which are prescribed

by the laws of the United States or by the State laws in force at the time of the filing of the petition in the State wherein they have had their domicile for the six months immediately preceding the filing of the petition, or for a longer portion of such six months than in any other State; Provided, however, that no such allowance shall be made out of property which a bankrupt transferred or concealed and which is recovered or the the transfer of which is avoided under this Act for the benefit of the estate, except that where the voided transfer was made by way of security only and the property recovered is in excess of the amount secured thereby, such allowance may be made out of such excess."

Section 47a(6). (11 U.S.C.A. 75a(6).)

"47. DUTIES OF TRUSTEES. a. Trustees shall . . . (6) set apart the bankrupt's exemptions allowed by law, if claimed, and report the items and estimated value thereof to the courts as soon as practicable after their appointment; . . ."

Section 70a. (11 U.S.C.A. 110a.)

"70. TITLE TO PROPERTY. a. The trustee of the estate of a bankrupt . . . upon his . . . appointment and qualification, shall . . . be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition in bankruptcy . . . except insofar as it is to property which is held to be exempt, . . ."

Section 70c. (11 U.S.C.A. 110c.)

"c. . . . The Trustee, as to all property in the possession or under the control of the bankrupt

> at the date of bankruptcy or otherwise coming into the possession of the bankruptcy court, shall be deemed vested as of the date of bankruptcy with all the rights, remedies, and powers of a creditor then holding a lien thereon by legal or equitable proceedings, whether or not such a creditor actually exists; . . ."

Under the provisions of these sections the following propositions appear to be clear beyond dispute:—

1. That the provision of the exemption laws, whether contained in the bankruptcy act or in state statutes, must be liberally construed—in the case of homesteads particularly for the purpose of protecting the family of the declarant.

Re Dudley (1947) 72 F. Supp. 943, particularly at 947, citing *Crawford v. Sternberg* (C.C.A. 8th 1915) 220 F. 73 at 76, reading:—

> "This has become an established principle, because the statutes granting exemptions have made no such exemptions, and because the policy of such statutes is to favor the debtors, in the limited amounts allowed to them, by preventing the forced loss of the home and of the necessities of subsistence, and because such statutes are construed liberally in favor of the exemption."

The *Dudley* case, supra, further is authority for the proposition that the claiming of an exemption through the device of purchasing exempt shares in a building and loan association, even while insolvent, cannot constitute a fraud upon creditors.

See also cases cited by Referee Wyman in his opinion (R.T. 25), including one decided by this circuit, *Dean v. Shephard* (C.C.A. 9) 26 F.2d 460, 461.

> "The rule prevailing in California is that once the homestead has been created, the objects of the law require that as a matter of social policy, to the end that the humane purposes which the Legislature intended by its enactment shall be effected, the homestead shall be protected to the fullest extent, and the power of a creditor to attack the homestead by forced sale must be strictly limited to the instances specified in the law."
>
> *Vieth v. Klett* (1948) 88 C.A.2d 23, at 27, 198 P.2d 314.

2. That the "State laws" of exemption or homestead which apply are those which are in effect at the time of the filing of the petition in bankruptcy and at no other time. Section 6 of the Act expressly so states.

1 Collier on Bankruptcy (14th Ed.) 816 and cases cited, citing principally *White v. Stump,* 266 U.S. 310, 45 S.Ct. 103, 69 L.Ed. 301, which said

> "that one common point of time is intended, and that is the date of the filing of the petition."

3. That there is authority two ways as to the meaning of the words "prescribed by the laws of the United States or by the State laws in force" at the time of the filing of the petition.

a. The expression "prescribed by law" has been given the meaning of the actual legislation upon the

subject. *Duran v. Pickwick Stages System* (1934) 140 C.A. 103, 108; *Exline v. Smith,* 5 C. 112, 113.

b. An alternative meaning has been given to the expression as including not only the statute but the decisions of the courts of the state interpreting the same. 1 Collier on Bankruptcy, supra, 796.

If the first of the two constructions were to apply to our situation, that would put an end to the problem because it would then be clear that at the time of the filing of the petition by bankrupt section 1260 of the California Civil Code provided for a homestead exemption of $12,500 over all liens and encumbrances. Hence a literal interpretation of section (6) would therefore require that the order of the Referee setting apart the homestead and the decision of the District Court should be sustained without further argument. While we urge this point upon this court, appellee feels that the second meaning can be accepted without weakening one bit the conclusion so reached.

4. That title to the homesteaded property does not at any time actually pass to the trustee or become a part of the bankrupt estate.

Section 70a of the Act, above quoted, states very clearly that title of the bankrupt passes to the Trustee *"Except insofar as it is to property which is held to be exempt"*. A terse summary of the rights of the Trustee with respect to exempt property is set out in 4 Collier on Bankruptcy 975, as follows (Section 70.08 thereof):

> "Exempt property constitutes one class of property that specifically does not pass to the trustee

under the Act. Section 70 provides that the trustee of the bankrupt's estate shall be vested with the title of the bankrupt 'except insofar as it is to property which held to be exempt'. This refers, of course, to the property declared exempt under § 6 of the Act, which section gives full effect to the exemption statutes of the states and the United States.

". . . It is sufficient to recall here that while the trustee does not take title, he does have a temporary right of possession in order to perform his duty of setting the exemption aside. The bankruptcy court has jurisdiction only for the purpose of determining the exemption and the merits of the bankrupt's claim, and may not adjudicate other claims thereto, or compel a sale unless the exempt and non-exempt property are indivisible. . . ."

See also: *Lockwood v. Exchange Bank* (1903) 190 U.S. 294, 23 S.Ct. 751, 47 L.Ed. 1061, where at page 1063, Justice White stated:—

"The fact that the act of 1898 confers upon the court of bankruptcy authority to control exempt property in order to set it aside, and thus exclude it from the assets of the bankrupt estate to be administered, affords no just ground for holding that the court of bankruptcy must administer and distribute, as included in the assets of the estate, the very property which the act, in unambiguous language declares shall not pass from the bankrupt, or become part of the bankruptcy assets. The two provisions of the statute must be construed together, and both be given effect. Moreover, the want of power in the court

of bankruptcy to administer exempt property is, besides, shown by the context of the act; since throughout its text, exempt property is contrasted with property not exempt, the latter alone constituting assets of the bankrupt estate, subject to administration.

"Though it be conceded that some inconvenience may arise from the construction which the text of the statute requires, the fact of such inconvenience would not justify us in disregarding both its letter and spirit. Besides, if mere arguments of inconvenience were to have weight, the fact cannot be overlooked that the contrary construction would produce a greater inconvenience. The difference, however, between the two is this: That in the latter case—that is causing the exempt property to form a part of the bankruptcy assets —the inconvenience would be irremediable, since it would compel the administration of the exempt property as part of the estate in bankruptcy; whilst in the other, the rights of creditors having no lien, as in the case at bar, but having a remedy under the state law against the exempt property, may be protected by the court of bankruptcy, since, certainly there would exist in favor of a creditor holding a waiver note, like that possessed by the petitioning creditor in the case at bar, an equity entitling him to a reasonable postponement of the discharge of the bankrupt in order to allow the institution in the state court of such proceedings as might be necessary to make effective the rights possessed by the creditor."

In the *Lockwood* case, supra, the Supreme Court held that even though a note of the bankrupt provided

for a complete waiver of his homestead rights, nevertheless the creditor could only assert his rights in the state courts since the bankruptcy act expressly negated the possibility of transfer of title to the Trustee or the jurisdiction of the bankruptcy court to administer exempt property as part of the estate assets, its only power being to determine that the exemption existed and setting it aside to the bankrupt. Many cases have since followed the doctrine of the *Lockwood* case, including the following more important ones:

Ingram v. Wilson (1903. C.C.A. 8th) 125 F. 913, at 915:

> ". . . never vested in the trustee and never became subject to administration . . . court was without power to order the sale of the homestead, and that its 'order to that effect was erroneous, if not void'; also that the creditor 'must seek such relief as he is entitled to under local laws in the courts of the state'. "

Re Remmerde (1913. D.C.-N.D. Ia.) 206 F. 822, at 826.

Re Vonhee (1916. D.C.-Wash.) 238 F. 422, at 428:

> "If any creditor has a specific claim upon any of this property, it must be enforced in the state court."

Duffy v. Tegeler (1927. C.C.A. 8th) 19 F.2d 305, at 308.

> "If creditors claim that the property, while exempt generally, is not exempt from process to enforce their particular debts, they must resort

to a state court of competent jurisdiction to enforce payment of their debts out of such property. On proper application, the discharge should be withheld for a reasonable time to enable such creditors to institute and prosecute the necessary proceedings in the state court to protect and make effectual their rights against the property."

Stein v. Bostian (1943. C.C.A. 8th) 133 F.2d 586, at 589.

"It may be true, as the referee points out, that the cash exemption set off to the bankrupt can be reached by his tax creditors through other proceedings, and that it would be convenient, expeditious and economical to have the court of bankruptcy order that the exemption be applied to the payment of the tax claims. That, however, does not alter the fact that Congress has not conferred upon the courts of bankruptcy jurisdiction to administer the exempt property of a bankrupt when a claim for exemptions has been filed, or to treat such property as any part of a bankrupt's estate."

"It was the duty of the trustee and of the court to safeguard the right of the bankrupt to his exempt property."

Woodruff v. Cheeves (1901 C.C.A 5th) 105 F. 601 —holding that the U. S. District Court is not entitled to entertain proceedings in the nature of a plenary proceeding to subject exempt homestead property to claims of certain creditors who held the bankrupt's notes which contained provisions waiving the benefit of the homestead laws.

As part of this proposition number 4 it may be observed that another facet thereof compels the conclusion that the bankruptcy court's control over exempt property is one of extremely limited nature.

Chicago, B. & Q. Co. v. Hall (1912) 229 U.S. 511, 33 S.Ct. 885, 57 L.Ed. 1306, at page 1309, described that control in these words:

> ". . . It is true that title to exempt property does not vest in the trustee, and cannot be administered by him for the benefit of the creditors. But it can 'pass to the trustee as a part of the estate of the bankrupt' for the purposes named elsewhere in the statute, included in which is the duty to segregate, identify, and appraise what is claimed to be exempt. He must make a report . . . In other words, the property is not automatically exempted, but must 'pass to the trustee as a part of the estate'—not to be administered for the benefit of creditors, but to enable him to perform the duties incident to setting apart to the bankrupt what, after a hearing, may be found to be exempt. Custody and possession may be necessary to carry out these duties, and all levies, seizures, and liens obtained by legal proceedings within the four months, that may or do interfere with that possession, are annulled . . . the liens rendered void by 67f are those obtained by legal proceedings within four months. The section does not, however, defeat rights in the exempt property acquired by contract or by waiver of the exemption. These may be enforced or foreclosed by judgments obtained even after the petition in bankruptcy was filed, under the principle de-

clared in Lockwood v. Exchange Bank, 190 U.S. 294, 48 L.Ed. 1061, 23 S.Ct. 751."

To the same effect:

Gardner v. Johnson (1952. C.C.A. 9th)—where held that referee could determine that failure to claim exemption at time of filing petition would constitute a waiver of the homestead; and further that her prior transfer of the homesteaded property to her daughter would in any event have constituted an abandonment thereof.

Appellant recognizes that the *Lockwood* case is still law (Brief, p. 4) but cites *Moore v. Bay* (1931) 284 U.S. 4, 76 L.Ed. 133, 76 A.L.R. 1198 to the effect that under the strong-arm provision of the Act the Trustee has the right to set aside a state given right of exemption as to certain creditors merely because as to another creditor the same right of exemption exists but in a smaller amount. Consideration will be given to this case in a later part of this brief, but it is sufficient to state at this point that the *Moore* case involves the matter of constructive fraud against creditors by failure to observe certain requirements of California Civil Code 3440, and does not touch upon or consider in any wise the application of the exemption provisions of the bankruptcy act.

5. If at the time of the filing of the petition in bankruptcy, the exemption is of the kind that constitutes an exemption generally, the setting aside of the exemption to the bankrupt is not impaired or pre-

cluded merely because also at that time some one creditor of the bankrupt has a right which permits him to assert rights in the property which could not be availed of by other creditors. In such cases, the bankruptcy court has no jurisdiction to determine such adverse claims or priorities therein, but does have the right to hold up a discharge in bankruptcy until resort is had to the state courts of competent jurisdiction to determine such adverse claims or priorities.

The foregoing proposition is a corollary to proposition number 4 above, and has been alluded to therein. The cases which support it are the same as those heretofore cited under that proposition number.

6. Section 70c of the Bankruptcy Act,—(11 U.S.C.A. 110c)—, which is the "strong-arm" provision of the Bankruptcy Act, "strong arms" the trustee in bankruptcy in exemption cases only for the purpose of determining if a valid homestead does or does not exist at the time of the filing of the petition in bankruptcy, or if there has been a conveyance of the homestead prior thereto which constituted an abandonment of the same, or a situation where elements of fraud exist which would destroy the right to the exemption and thus make the property available for the whole estate.

An early case called upon to deal with this specific subject was decided by this very Court of Appeals (9th Circuit) in 1914 in the case of *Brandt v. Mayhew,* 218 F. 422. At that time under the laws of California a homestead could be declared upon real property even after the filing of the petition in bank-

ruptcy, which was done by the wife of the bankrupt after they had jointly made general assignment for the benefit of creditors, which included the property described in the homestead subsequently filed. The bankrupt made claim to the homestead on the basis of his wife's filing which the trustee denied, but which the referee allowed. The trustee on appeal from order of the District Court affirming the referee contended that the "strong-arm" provision (then section 47a(2)) superseded the provisions of section 6 (still the same) and those of the first part of section 70a (still the same excepting exempt property from vesting in the trustee) and being in the position of a lien creditor could set aside the exemption in its entirety. On page 426 of 218 F., Judge Gilbert denied this and for the court stated:—

> "The argument is that the amendment puts the trustee, as to all property in the custody of the bankruptcy court, in the position of a creditor holding a lien by legal or equitable proceedings, and, as to all other property, in the position of a creditor holding an execution returned unsatisfied, and that it follows that the trustee in the case at bar is in the attitude of a lien creditor as to the real estate which is claimed as a homestead, and that his lien represents the entire indebtedness against the bankrupt, so as to exclude a claim of homestead exemption. We do not so construe the amendment. Section 6 of the act remains unamended and unrepealed. The amendment does not affect the provision of that section, in which the intention of Congress is plainly expressed, that the Bankruptcy Act shall not affect the allowance to bankrupts of the ex-

> emptions which are prescribed by state laws. Section 6 still remains one of the fundamental provisions of the act, and it is the duty of the courts to construe the act with all its amendments as a whole, and to harmonize all its parts. The purpose of the amendment to 47a was to make effective the rights of creditors against those who claimed secret or unrecorded liens or adverse interests in the property of the bankrupt. Before the amendment was vested with no better title to the bankrupt's property than the bankrupt had at the time when the trustee's title accrued. He stood in the shoes of the bankrupt, and where, under the law of the state, a conditional sale, a vendor's lien, or an unrecorded mortgage was good between the parties, it was good against the trustee. The amendment gives the trustee the right to attack all such unrecorded liens and secret equities, without requiring that he shall be in the position of representing creditors who have acquired liens by legal or equitable proceedings against the bankrupt . . ."

A case of recent decision by this 9th Circuit which considered the effect of section 70c and its application to a situation where the claim of homestead was filed AFTER the filing of the petition in bankruptcy is that of *Sampsell v. Straub* (1951. Cert. Den. 1952) 194 F. 2d 228, cited by appellant (Brief, p. 4). This court there determined solely that the trustee with the powers given him under section 70c could attack the recording of a homestead AFTER date of bankruptcy because he stood in the position of a creditor who had a judgment lien prior in time thereto at the

time of the filing of the petition, even though the judgment lien must be perfected by the doing of a voluntary act by the judgment creditor, namely the filing of an abstract of judgment. The net result of the decision was to hold that no exemption in fact existed at all at time of filing of petition in bankruptcy, and that therefore the property was properly part of the bankrupt estate. The circumstances there are completely different from the case at bar where no question has been raised herein about the validity or timing of the recording of the declaration of homestead by Mr. Sanderson. There is no suggestion of fraud, direct or constructive, against any creditors. It follows therefore that the law and procedure above mentioned under propositions numbered 4 and 5 still apply and must be followed. Nor does *Moore v. Bay,* supra, compel any contrary conclusion. That case on its face, clearly establishes a fraud situation and therefore under section 67 of the Bankruptcy Act the trustee had the right to set aside the chattel mortgage,—as to which the procedure of Civil Code 3440 had not been followed,—as a constructive fraud and declare it void in toto as against all creditors. No exemption rights were involved or considered in that case.

From the foregoing propositions, a logical development of those principles results in the following result and no other:—

That the general exemption of the homestead declared by Mr. Sanderson existed at the time of the filing of his petition in bankruptcy which entitled

him to assert as to all creditors except one an exemption of $12,500, and as to only one an exemption of $7,500. There being no element in the case at bar of improper, invalid, or fraudulent declaration of homestead, no element of waiver, abandonment, or fraudulent preference within four months of bankruptcy involved, the sole duty of the trustee, after determining values and items making up the exemption, was to so report to the referee in bankruptcy, and the sole jurisdiction of the bankruptcy court was to order the exemption set aside. If necessary, on application of the one creditor who might be entitled to assert rights in the smaller amount of homestead (which at all times existed and was in effect as to all creditors) the bankruptcy court could have stayed Mr. Sanderson's discharge until that creditor's rights had been so declared in the state courts. But beyond this, the jurisdiction of the bankruptcy court was exhausted.

II. APPELLANT'S ARGUMENT IS NOT PREDICATED UPON FIRM GROUND.

The appellant states (Brief, pp. 4-14) that the homestead can not be set aside and the rights of the creditors claiming special treatment should not be determined in the state courts because:—

(1) The increased amount of exemption from $7,500 to $12,500 at the time that one creditor was existing to that extent constituted an impairment of the obligation of contract as to that one creditor so involved, and that as to that creditor the bankrupt

was left with only an exemption of $7,500 rather than $12,500; and

(2) (Step number 2)—Under section 70c of the Bankruptcy Act the trustee in bankruptcy can "strong-arm" the situation into one where he can assert that as to ALL creditors the same limitation existed—even though it might be recognized that under California law there is no question but that the homestead is valid and in full force and effect as to ALL creditors in the larger sum except the one creditor previously mentioned.

For the first of the foregoing propositions, appellant relies upon the decision of *In re Rauer's Collection Co., Inc.* (1948) 87 C.A. 2d 248, 196 P. 2d 803, (Brief, p. 5); *In re Fox* (D.Ct.So.D.Cal. Yankwich 1936) 16 F. Supp. 320 (Brief, p. 8); *Smith v. Hume,* 29 C.A. 2d 747, 74 P. 2d 566 (Brief, p. 12) and certain decisions of the Referee in Bankruptcy of the U.S. Dist. Ct. for the Southern District (Brief, pp. 12-13); *The Queen* (D.Ct.N.D.-Cal.) 93 F. 834 (Brief, p. 13), all of which hold that as to a particular creditor an exemption increase by statute is to the extent of the increase an impairment of the obligation of contract as to existing creditors. But the holding that an obligation of contract is impaired as to a particular creditor does not impel a decision that a part of the exemption of the homestead is lost as to all creditors, either by logic or by clear implication of the Bankruptcy Act.

In the first place it may be observed that the objects of the prohibition against the impairment of

obligation of contract contained in the Federal Constitution (Article I, section 10) are the States themselves, not the Federal government. The California Constitution (Article I, section 16) carries the same provision, self-imposed. There is no prohibition anywhere in the Federal Constitution against Congress acting through authorized legislation—(Federal Constitution Article I, section 8, subsection 4—establishing uniform bankruptcy laws)—to do all things necessary to carry out the purposes thereof, even though the obligation of contracts is impaired.

> "Bankruptcy Acts avowedly work an impairment of the obligation of contracts, especially where they contemplate a discharge of the debtor from his debts. The provision of the Constitution of the United States that no state shall pass any law impairing the obligation of contracts is, in its terms, a limitation on the powers of the states only, and neither it nor any other clause forbids the Congress of the United States, when acting within the scope of its powers, to enact laws which may operate to impair the obligation of contracts. The grant of power to Congress to legislate on the subject of bankruptcies includes the power to impair the obligations of contracts, notwithstanding the individual states are forbidden so to do. Legislation may be valid as enacted under the express power to establish uniform laws on the subject of bankruptcy, although framed and drawn for the direct purpose of relieving insolvent persons in whole or in part from the payment of their debts. Congress, while without power to impair the obligation of contracts by laws acting directly and independ-

> ently to that end, undeniably has authority to pass legislation pertinent to any of the powers conferred by the Constitution, irrespective of a collateral or incidental effect of the legislation to impair or destroy the obligation of private contracts. The constitutional provision conferring upon Congress the power to legislate on the subject of bankruptcy is read into contracts as constituting a part thereof . . ."
>
> 6 Am.Jur. 554, 555, Bankruptcy, section 7.

When therefore we assert that the *Rauer Collection* case, heretofore cited, does not necessarily control because it does not involve bankruptcy proceedings, but only a matter of interpretation of state laws in state courts (see Appellant's Brief, p. 5) we believe we are making a valid and important distinction. Valid,—because the impairment of obligation prohibition was binding upon the California Supreme Court and the Court was perforce compelled to interpret state laws apart from any consideration of bankruptcy matters (a Federal matter) in which Congress may validly authorize such impairment; and Important,—because section 6 of the Bankruptcy Act expressly states that the law *in effect at the time of filing the petition in bankruptcy* controls the exemption. If this includes not only the exemption but the amount, then the only logical conclusion is that the exemption of the homestead exists in the sum of $12,500 for all purposes, even though it might have the effect of increasing the exemption as to the pre-existing creditor himself. In other words, once the bankrupt goes into the Federal Court and petitions

in bankruptcy and asserts his exemption, any creditor of his is affected immediately by the provisions of the bankruptcy act and the only result, upon an exact and literal reading of section 6 of the act (supplemented by such cases as *Duran v. Pickwick Stages System* (1934) 140 C.A. 103 and *Exline v. Smith,* 5 C. 112, which define "prescribed by law" as only to embrace statutory law), would be that he is entitled to the exemption then "in force" of $12,500 and nothing less, and this even though a creditor who might be entitled to some sort of priority under state law in the homesteaded property and as to which his right or priority would necessarily be impaired. Therefore to state that the increase of exemption constituted an impairment of obligation of contract under state law, and ergo, that under the bankruptcy act the impairment must be recognized, is to make a false assumption. Otherwise, the words "in effect" are meaningless. And to disregard the *Rauer* decision on the ground that while it may be a proper decision in so far as it may apply to state action and to the respective rights of creditors in homesteaded property when asserted in state courts and in state proceedings is not necessarily doing violence to the construction of the bankruptcy act which by section 6 unqualifiedly declares the bankrupt to have all those exemptions "prescribed by" the laws of California—in this case, the full measure of statutory rights under Civil Code Section 1260.

But it is not necessary to rest our argument on that ground alone. Even assuming that the "laws of Cali-

fornia'' which are referred to in section 6 of the Bankruptcy Act mean the statute (C.C. 1260) plus the *Rauer* and other decisions interpreting the same, yet it does not follow that the second proposition asserted by the appellant is validly grounded.

First, as heretofore noted in this brief, section 70c of the Act does not supersede or annul or modify section 6 of the Act. It must be considered in light of the provisions of section 6 and the purposes of section 6, about which we have heretofore rather fully alluded under proposition 6 of section I of this brief, together with authorities cited.

Secondly, section 70c was not enacted to destroy valid exemptions which are not subject to attack for fraud, waiver, abandonment, invalidity and similar grounds which equitably and properly require the property which is claimed to be exempt to become part of the bankrupt estate. For example in the case of *Sampsell v. Straub,* decided by this court in 1951, heretofore cited, this court determined that since the homestead was not claimed within time it should not be recognized at all. That does not present the same situation as in the case at bar, because in the *Sampsell* case it was correctly held that the late recording of the homestead had no validity at all against all creditors, there being none who had any special rights, and none who existed after a valid homestead might have been claimed, whereas in our case we have a validly claimed homestead which is acknowledged to be good against both prior creditor and subsequent creditors, the only contention being that as to the prior creditor

he might be able to assert some additional right which the state laws recognize as against the subsequent ones. In our case there is no suggestion of any waiver, abandonment or other weakness which in any degree would affect or destroy the homestead which existed at the time of the filing of the petition in bankruptcy.

What the trustee in bankruptcy in effect is attempting to accomplish is to assert that since the $7,500.00 amount is the maximum limitation as to one creditor it must stand in the bankruptcy proceedings as the maximum limitation as to all creditors of the bankrupt. This, even though the same result would not obtain under state law. The incongruity of such a result is immediately apparent. Such a result would not carry out the purposes of the Bankruptcy Act, but in fact would actually violate its spirit and intent—which is to give relief to debtors entitled thereto—by giving greater rights to the creditors of a bankrupt in exempt property (those who became such subsequent to the increase of the homestead exemption, and therefore valid and enforceable as to them under the *Rauer* decision) than they possessed under state law at the time of the filing of the petition in bankruptcy. Thus this construction would permit the enforcement of laws which are NOT those "in effect at the time of the filing of the petition in bankruptcy" which section 6 of the Bankruptcy Act expressly requires. To adopt an expression of Judge Yankwich in the *Dudley* case, 72 F. Supp. 943, 947, this would mean reading into the statute "restrictions which are not there. And this we cannot and should not do."

We find the purpose of section 70c tersely explained by this court (9th Circuit) in the *Sampsell* case (*Sampsell v. Straub,* 194 F. 2d 228), where at page 231 we read:

> "Section 70, sub. c on the other hand is employed primarily to protect general creditors of the bankrupt against secret liens. To this end the trustee is given all the rights which a lien creditor by legal or equitable proceedings would enjoy."

Thus the intent of section 70c is to put the trustee in position to avoid transfers or claims of interest which would be in the nature of fraud or inequity to assert against creditors or the estate. We have no such considerations in the case at bar.

It is submitted therefore that the argument of the appellant loses force and validity when considered in the light of the foregoing discussion and authorities cited.

III. THE DISTRICT COURT DID NOT ERR IN DETERMINING (T.R. 67) THAT THE REMEDY OF CREDITORS WHOSE RIGHTS UNDER CALIFORNIA LAW EXTENDED BEYOND THE $12,500.00 EXEMPTION IS IN THE STATE COURTS.

In keeping with the principle which has been repeatedly announced in the Federal Courts, the cases respecting which have been cited heretofore in this brief under proposition number 4 of point I of Argument, and also alluded to in proposition number 5 thereof, title to Mr. Sanderson's homestead never at any time passed to the trustee in bankruptcy herein for the purpose of general administration in this

bankrupt estate. To the cases heretofore cited should also be mentioned the following:

Re Carl (D.Ct. Ark. 1941) 38 F. Supp. 414;

Baumbaugh v. L. A. Morris Plan Co. (C.C.A. 9th) 30 F. 2d 816;

Re Buckley (D. Ct. La.-1938) 24 F. Supp. 832 and cases cited on page 835 thereof.

As a direct corollary thereof it followed, as these cases determined, that since the bankruptcy court had no jurisdiction to determine claims of priority in exempt property it could only hold up the discharge of the bankrupt until the matter had been determined in the state court and then determine the extent of the discharge to which the bankrupt was entitled.

Appellant states (Brief, p. 15) that the *Buckley* case clearly held that the trustee could sell the exempt property where the fair value exceeded the exemption. The *Buckley* case did not so "clearly hold" or hold at all to that effect. The case determined that where the referee had ordered a sale of the exempt property the "ruling of the Referee was erroneous and that all this court has jurisdiction to do is to direct the trustee to set aside the property scheduled as exempt, leaving the creditor Wyatt to his remedies in the State Court." (p. 835 of 24 F. Supp.) Creditor Wyatt there claimed a priority by mortgage in the exempt property. In its treatment of the situation, the court, p. 834, stated:

> "The title to the property exempt under the laws of the State does not pass to the trustee, and it

> is his duty, when claimed, to set it aside as such when it becomes clear that the bankrupt is a person entitled to claim it, as here, and the fair value of the property does not exceed the amount allowed by the State law. The bankruptcy court has jurisdiction only for the purpose of determining these matters and cannot require its sale, even on the petition of creditors holding a waiver, or otherwise entitled to compel the application of the exempt property to the satisfaction of their claims."—citing many cases.

This was followed by the *Carl* case, supra, and by Judge Murphy in the court below, and we submit rightly so.

CONCLUSION.

For the foregoing reasons, we respectfully submit that the decisions of Referee Wyman and of Judge Murphy were both correct, and that they can be sustained either on the ground that:

1. Under section 6 of the Bankruptcy Act, the law in effect at time of the petition in bankruptcy specified a homestead exemption of $12,500.00 without exception as to any creditor; or

2. If as to any one creditor the maximum amount of the homestead exemption under the law of California could only be asserted in a lesser sum than specified by statute at the time of the filing of the petition in bankruptcy, his remedy was to ask the bankruptcy court to hold up the discharge of the bankrupt for a reasonable time until he could go into

the state courts to determine his rights, the state courts being the only forum in which he could assert the same.

Dated, San Francisco, California,
May 7, 1956.

Respectfully submitted,
JEFFERSON E. PEYSER,
Attorney for Appellee.

LEONARD S. LURIE,
Of Counsel.